

## MINING BLOG

### DIAMOND ROYALTIES IN ONTARIO (Part 2)

In addition to the diamond royalty payable to the Government of Ontario pursuant to section 154 of the *Mining Act* (Ontario), an owner of a diamond property in Ontario (as in other jurisdictions) may grant royalties to third parties in respect of the production of diamonds on the property.

It must be emphasized that there are no "standard" definitions of royalties in the mining industry. Each royalty agreement must be carefully reviewed as the definitions of revenues, expenses and other material terms may change dramatically depending on the circumstances. Examples of diamond royalties are set out below.

#### Gross Overriding Diamond Royalty

A gross overriding diamond royalty typically entitles the royalty holder to receive a payment equal to a specified percentage of the "average appraised value" of all gem and industrial diamonds recovered, sorted and graded from the property (collectively, "diamonds"), free and clear of all costs of development and operation and subject only to mineral and mining taxes, royalties and the fees and expenses of graders. The term "average appraised value" may be defined to mean the average of the valuations of the diamonds at the mine site determined by two independent graders, one appointed by the owner of the property and one appointed by the holder of the royalty. Such independent graders should be duly qualified and accredited and are responsible to sort, grade and value the diamonds in accordance with industry standards, having regard to such factors as the commercial demand for the diamonds, the grades of the diamonds (gem or industrial) and the colours, sizes and clarity of the diamonds. Each independent valuator is required to value each particular classification of the diamonds in accordance with industry pricebooks, standards and formulas. A gross overriding royalty is typically paid to the royalty holder on this basis, regardless of the price or proceeds actually received in connection with the diamonds or the manner in which a sale of the diamonds to a third party is made, without deduction except for taxes and other royalties. The owner will calculate and pay the gross overriding royalty to the holder within a specified time period after the end of each calendar quarter, based on all diamonds from the property which were graded in such calendar quarter. The royalty holder will not be entitled to participate in the profits or be obligated to share in any losses generated by the owner's actual marketing or sales practices.



Michael G. Hobart, Partner  
[mhobart@foglers.com](mailto:mhobart@foglers.com)  
416.941.8856

Michael Hobart is a partner in the Business Law Group's Securities department.

Fogler, Rubinoff LLP  
Lawyers  
77 King Street West  
Suite 3000, P.O. Box 95  
TD Centre North Tower  
Toronto, ON M5K 1G8

Tel: 416.864.9700  
Fax: 416.941.8852

[foglers.com](http://foglers.com)

### Net Proceeds Diamond Royalty

A net proceeds diamond royalty typically entitles the royalty holder to receive a specified percentage of the proceeds received from the sale of diamonds mined from the property less the aggregate of all costs related to the sorting, valuing, shipping and insurance of such diamonds, including salaries of personnel engaged in performing such services. The meaning of these words should be precisely set out to avoid disputes. The following definitions may be considered when drafting a diamond royalty agreement:

"*sorting*" means the separation of the diamonds from waste materials and the dividing of them into groups according to quality, size, and/or other characteristics and then the dividing of such groups into appropriate lots or groups for valuing and/or sale, it being acknowledged that in the case of gem quality diamonds a group or lot may be a single stone.

"*valuing*" means the establishing of a value for each lot or group of sorted diamonds for purposes of reference when negotiating with a potential purchaser.

"*shipping*" means all methods or places of transportation and/or storage of diamonds from the moment they leave the mine or treatment facilities at the property until the passing of title thereto or risk therefor (whichever is the later) to a purchaser or purchasers, including, without limitation, any cost that may be incurred by reason of such methods or places used or any sorting or valuing facilities being situated off the property.

"*insurance*" means all insurance that the operator considers advisable to protect all or part of the diamonds in the possession or control of the operator (including, without limitation during shipping) until the passing of title thereto and risk therefor to a purchaser or purchasers, including, without limitation, the insurance or bonding of any person who does or may come into contact with any such diamonds at any point during the operations of the operator, whether such person is an employee of the operator or otherwise, all as the operator considers advisable in the circumstances from time to time.